

Implications of the Federal Right of Rescission for Lenders and Borrowers

**An Interactive Day of Building an Effective
Community Response to Foreclosures in Wisconsin**

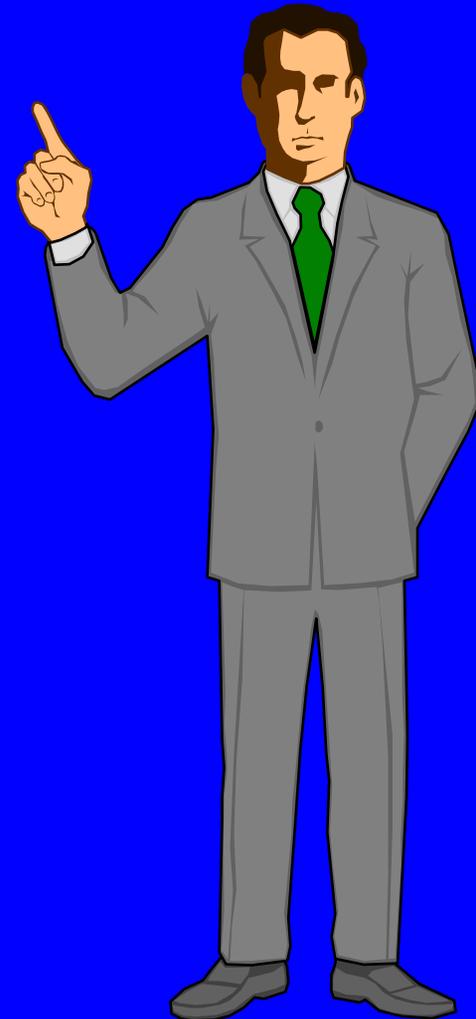
December 12, 2007

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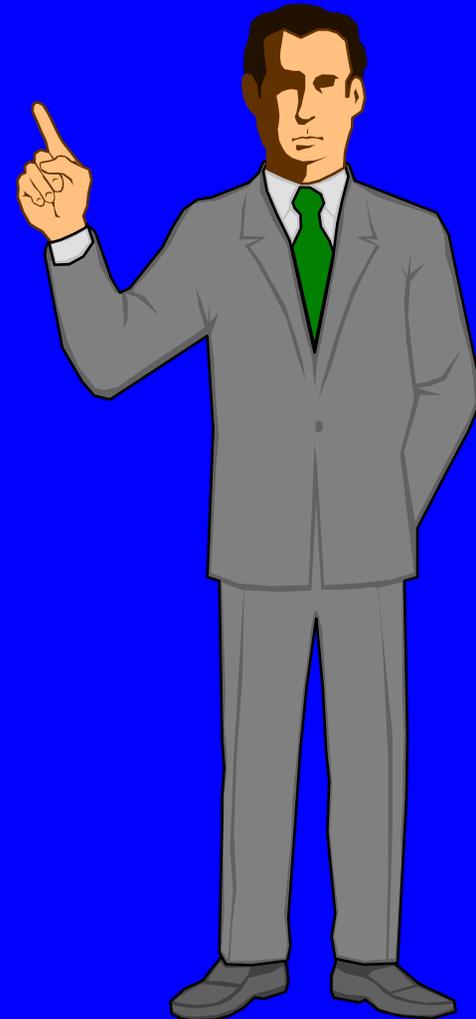
Today's Program

- **Introduction –
why is this
important?**
- **Purpose of the
TILA and Reg Z**
- **Structure of the
law**
- **What is the right
of rescission?**



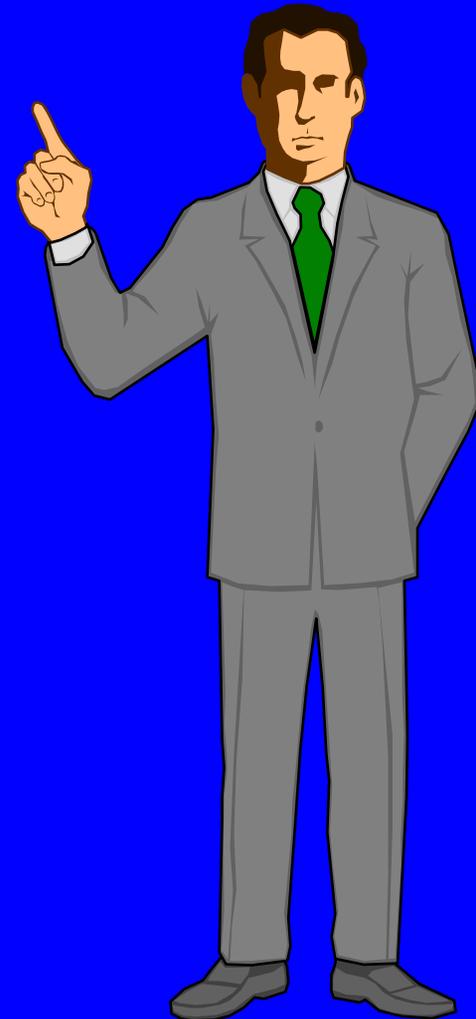
Today's Program

- **What kind of loan is rescindable?**
- **Who is able to rescind a loan?**
- **Requirements for lenders**
- **What are material disclosures?**
- **Rescission clock**

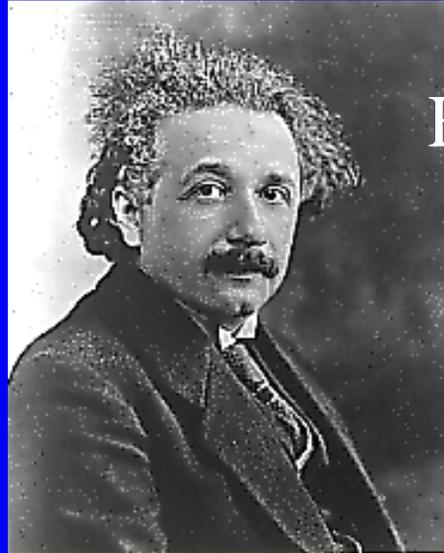


Today's Program

- **Waiving the right**
- **Effects of rescission**
- **Assignee liability**
- **Questions????**



BIG DEAL



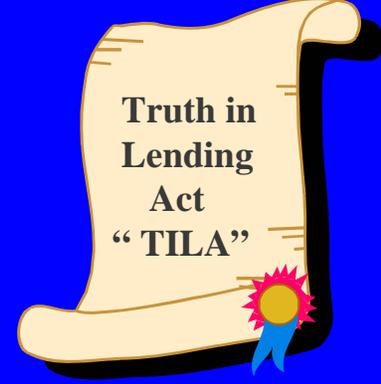
$$E = mc^2$$

Albert Einstein

He never had to figure out Reg Z compliance

Truth in Lending Act

“TILA”



- TILA was enacted in 1968, 15 USC 1601 et seq., as title I of the Consumer Credit Protection Act (Pub. L. 90-321). Its purpose was to ensure that credit terms were disclosed in a meaningful way to consumers.
- The TILA, implemented by Regulation Z (12 CFR 226), became effective July 1, 1969.

Structure of the Law

- TILA is found at 15 USC 1601 – 1693r;
- Regulation Z is found at 12 CFR part 226;
- The Official Staff Commentary is found at Supp I of Regulation Z.

What is the Right of Rescission?

- A consumer protection law that allows consumers the opportunity to reconsider certain obligations for 3 business days after the loan is closed;
- During the “cooling off” period, consumers are free to change their minds and rescind (cancel) the loan for any reason;
- When the transaction is rescinded, all parties must be returned to their pre-transaction position and the transaction is cancelled.

To Determine Whether the Rule Applies – Ask Three Questions

- First, Does Reg Z apply to the transaction?
- Second, is the loan secured by a consumer’s “principal dwelling?”
- Third, is the transaction to purchase the dwelling?

What kind of loan is rescindable?

- The Right of Rescission applies to non-purchase money, Reg Z loans in which a security interest is taken in a consumer's principal dwelling. For example:
 - Home equity line of credit
 - An installment loan where the borrower pays a fixed amount and repays the debt on an agreed payment schedule
 - A security interest that is acquired by a contractor who is also extending credit in the transaction

Types of Non-rescindable Loans

- A loan to purchase or build the consumer's principal dwelling (i.e., a residential mortgage transaction).
- A consolidation or refinance with the same lender who already holds the mortgage and no additional funds are borrowed.
- A business-purpose loan, even though the loan is secured by the customer's principal dwelling.
- A transaction in which a state agency is a creditor.
- A mechanic's lien where the contractor is not a party to the credit transaction.

Cash-out Refi Rules

- Here, the consumer is refinancing more than they owe on their current mortgage and taking the difference out in cash.
- For a cash-out refinancing with the same lender, only the cash-out portion is subject to the right of rescission.
- For a cash-out refinancing with a different lender, the entire loan amount can be rescinded.

Structure must be Consumer's Principal Dwelling

- A consumer can only have one principal dwelling at a time.
- A vacation or other second home would not be a principal dwelling.
- A transaction secured by a second home that is not currently being used as the consumer's principal dwelling is not rescindable, even if the consumer intends to reside there in the future.
- When a consumer buys or builds a new dwelling that will become the consumer's principal dwelling within one year, it is considered the principal dwelling if it secures the construction loan.

Who is able to Rescind a Loan?

- The Right of Rescission doesn't apply to just borrowers. All consumers who have an ownership interest in the property have the right to rescind.

Rescission Period

- The period within which the consumer may exercise the right to rescind runs from 3 business days from the last of three events:
 - Consummation of the transaction
 - Delivery to the consumer of the required rescission notice
 - Delivery of all material disclosures

Unexpired Right of Rescission

- When the creditor has failed to take the action necessary to start the rescission period running, the right automatically lapses on the occurrence of the earliest of the following 3 events:
 - Expiration of **THREE YEARS** after consummation
 - Transfer of all the consumer's interest in the property
 - Sale of the consumer's interest in the property

Practical Consequences of the Right of Rescission

- There are two separate rights to rescind:
 - First, consumers can exercise their 3 day right to cancel after the loan documents are signed.
 - Second, there is an extended right to rescind if the consumer is not provided with the proper notice or the material disclosures are not accurate.

Special Rules for Foreclosures

- After initiation of foreclosure on the consumer's principal dwelling that secures the loan, the consumer can rescind if:
 - A mortgage broker fee that should have been included in the finance charge was not included; or
 - The creditor did not provide the right of rescission notice.

Right of Rescission Requirements for Lenders

- Lenders must provide certain “*material disclosures*” and multiple copies of the right of rescission notice to EACH owner of the property.
- After providing all proper disclosures, lenders must wait at least 3 business days before disbursing loan proceeds.

H-8—Rescission Model Form (General)

NOTICE OF RIGHT TO CANCEL

Your Right to Cancel

You are entering into a transaction that will result in a (mortgage/lien/security interest) (on/in) your home. You have a legal right under federal law to cancel this transaction, without cost, within three business days from whichever of the following events occurs last:

- (1) _____, the date of the transaction, which is _____; or
- (2) the date you received your Truth in Lending disclosure; or
- (3) the date you received this notice of your right to cancel.

If you cancel the transaction, the (mortgage/lien/security interest) is also cancelled. Within 20 calendar days after we receive your notice, we must take the steps necessary to reflect the fact that the (mortgage/lien/security interest) (on/in) your home has been cancelled, and we must return to you any money or property you have given to us or to anyone else in connection with this transaction.

You may keep any money or property we have given you until we have done the things mentioned above, but you must then offer to return the money or property. If it is impractical or unfair for you to return the property, you must offer its reasonable value. You may offer to return the property at your home or at the location of the property. Money must be returned to the address below. If we do not take possession of the money or property within 20 calendar days of your offer, you may keep it without further obligation.

How to Cancel

If you decide to cancel this transaction, you may do so by notifying us in writing, at

lender's name and business address.

You may use any written statement that is signed and dated by you and states your intention to cancel, _____ or you may use this notice by dating and signing below. Keep one copy of this notice because it contains important information about your rights.

If you cancel by mail or telegram, you must send the notice no later than midnight of _____ (or midnight of the third business day following the latest of the three events listed above). If you send or deliver your written notice to cancel some other way, it must be delivered to the above address no later than that time.

I WISH TO CANCEL

Consumer's Signature

Date

What are the Material Disclosures?

- An accurate and complete Truth in Lending Disclosure Form.
- Disclosure must include the APR, finance charge, amount financed, and total of payments.
- Other necessary disclosures include the number of payments to be made over the life of the loan and the regular payment amount.

ANNUAL PERCENTAGE RATE The cost of your credit as a yearly rate <p style="text-align: center;">%</p>	FINANCE CHARGE The dollar amount the credit will cost you <p style="text-align: center;">\$</p>	Amount Financed The amount of credit provided to you or on your behalf <p style="text-align: center;">\$</p>	Total of Payments The amount you will have paid after you have made all payments as scheduled <p style="text-align: center;">\$</p>	Total Sale Price The total cost of your purchase on credit including your downpayment of <p style="text-align: center;">\$ _____</p>
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You have the right to receive at this time an itemization of the Amount Financed.

- I want an itemization. I do not want an itemization.

Your payment schedule will be:

Number of Payments	Amount of Payment	When Payments Are Due

Insurance

Credit life insurance and credit disability insurance are not required to obtain credit, and will not be provided unless you sign and agree to pay the additional cost.

Type	Premium	Signature
Credit Life		I want credit life insurance _____ Signature _____
Credit Disability		I want credit disability insurance _____ Signature _____
Credit Life and Disability		I want credit life and disability insurance. _____ Signature _____

You may obtain property insurance from anyone you want that is acceptable to _____ If you get the insurance from _____ you will pay \$ _____.

Security: You are giving a security interest in:

- the goods or property being purchased.
 (and acquisition of other property).

Filing fees \$ _____ Non-filing insurance \$ _____

Late Charge: If a payment is late, you will be charged \$ _____ / _____ % of the payment

Prepayment: If you pay off early, you

- may will not have to pay a penalty.
 may will not be entitled to a refund of part of the finance charge.

See your contract documents for any additional information about nonpayment, default, any required repayment in full before the scheduled date, and prepayment refunds and penalties.

* means an estimate

TILA Disclosures Must Be Accurate

- Accuracy relies on two elements:
 - Finance Charge
 - Annual Percentage Rate, the “APR”

Finance Charge Accuracy

- If the borrower is seeking to rescind and the lender has not started foreclosure proceedings – the tolerance is one-half of one percent (.005).
- If the lender has started foreclosure proceedings, the tolerance is \$35.
- If the lender overstates the Finance Charge, there is no extended right to rescind.

Annual Percentage Rate – APR Accuracy

- Tolerance for the APR disclosed in the TILA Disclosure is one-eighth of one percent (.00125).
- The APR is inaccurate if it exceeds or is lower than the true APR by .00125 (see Commentary 226.22(a)(2)-1).
- One-eighth of one percent (.00125) accuracy tolerance applies to “regular” transactions.

APR Accuracy for “Irregular” Transactions

- One-fourth of one percent (.0025) accuracy tolerance applies to “irregular” transactions.
- An “irregular” transaction is one that has either multiple advances, irregular payment methods, or irregular payment amounts (other than an irregular first or final payment). Commentary 226.22(a)(2)-1.

How to Calculate Tolerances?

- **APR Calculator program offered by the Office of the Comptroller of the Currency (OCC)**
- **Available on the internet at:
<http://www.occ.treas.gov/aprwin.htm>**
- **Available for purchase for \$20 or free if you download it!!!**

Right of Rescission Time Clock

- 3 day rescission period begins once the notice and material disclosures have been given, and lasts three FULL business days.
- Business days are defined by Reg Z to include ALL calendar days except Sundays and federal holidays.
- Saturday IS considered a business day for rescission purposes, regardless of whether your business offices are open.

Calculating an Example

- Assume a closing is set for Thursday, September 6, 2007, and that all material disclosures and notices are provided to the parties at closing.
- The rescission period would run:
- Friday, September 7, 2007;
- Saturday, September 8, 2007; and
- Monday, September 10, 2007.
- Rescission period ends at midnight on September 10, 2007.

Waiving the Right of Rescission

- Borrowers can waive their rights, but on an exception basis only.
- Borrowers can waive their right and receive loan proceeds immediately, only if they have a “bona fide personal financial emergency.”
- This means a financial emergency so serious that waiting an additional 3 business days for the loan proceeds will be personally or financially devastating to the borrower.
- In order to waive the right, the borrower must provide a written explanation of the bona fide personal financial emergency to the lender.
- This is not a document that the lender should draft for the borrower.

Disbursing After the Rescission Period is Over

- Once the rescission period has expired, the lender must be reasonably certain the borrower has not rescinded the transaction before it disburses the loan proceeds.
- The law allows borrowers to exercise their rescission rights by mail – and a rescission is effective when mailed.
- Be sure to confirm that all owners have not exercised their rescission rights.

A Word about HOEPA Loans

- TILA was amended in 1994 to add the Home Ownership and Equity Protection Act.
- The main purpose of the law was to protect consumers from predatory lending practices.
- The law imposed new disclosure requirements and substantive limitations on certain closed-end mortgage loans bearing rates or fees above a certain percentage or amount.
- Failure to provide properly completed HOEPA Disclosures or use of a prohibited loan term can create an extended right to rescind the loan.

Rescission Process

Notifying the Lender

- Borrower must notify the lender, in writing, of the cancellation of the loan.
- Notice can be transmitted by mail, telegram, or other means.
- It should be sent to the lender's designated place of business.
- A rescission notice sent by the borrower's attorney is also effective.
- When the lender fails to provide an address to send the rescission notice, delivery to the servicer will be effective notice as to the lender or its assignee.

Relationship between Servicer and Creditor

- 15 USC section 1641. Liability of assignees
- (f) Treatment of servicer
 - (2) ... Upon written request by the obligor, the servicer shall provide the obligor, to the best knowledge of the servicer, with the name, address, and telephone number of the owner of the obligation or the master servicer of the obligation.

Effects of Rescission

- Once a consumer rescinds a transaction, the security interest becomes void and the consumer is not liable for ANY amount, including finance charges.
- Within 20 calendar days after receipt of a notice of rescission, the creditor shall return any money or property that has been given to anyone in connection with the loan.
- The lender must take steps to terminate the security interest.
- Once the lender has performed as above, the consumer must tender any money received back to the lender.
- Once tender is delivered, rescission is complete.

Assignee Liability

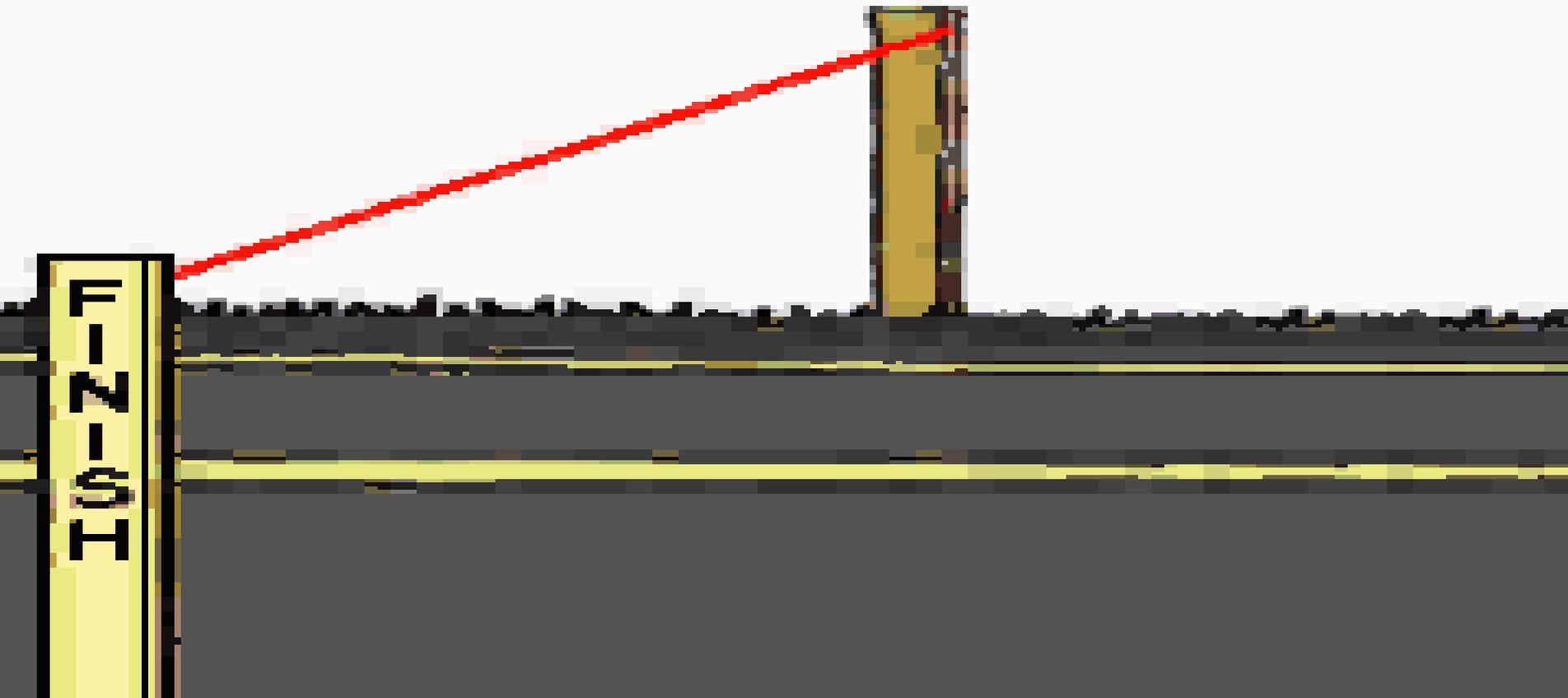
- 15 USC section 1641. Liability of assignees
- (c) Right of rescission by consumer unaffected – Any consumer who has the right to rescind a transaction under 15 USC 1635 of this title may rescind the transaction as against any assignee of the obligation.

Assignee Liability - Servicers

- 15 USC section 1641. Liability of assignees
- (f) Treatment of servicer
 - (1) In general – a servicer of a consumer obligation arising from a consumer credit transaction shall not be treated as an assignee of such obligation for purposes of this section unless the servicer is or was the owner of the obligation.

That's our finish!

Any Questions?



Contact Information

Steve Kuehl

Consumer Regulations Director

Federal Reserve Bank of Chicago

Consumer & Community Affairs - 11th Floor

230 South La Salle Street

Chicago, IL 60604-1413

steven.w.kuehl@chi.frb.org

Direct: (312) 322-5015

Fax: (312) 913-2626